(36)

IN THE

Supreme Court of the United States

October Term, 1942

No. 220

Trinity Corporation, *Petitioner*,

v.

Commissioner of Internal Revenue, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The above-named petitioner, by its counsel, prays that a writ of certiorari issue to review the judgment entered against the petitioner by the United States Circuit Court of Appeals for the Fifth Circuit in the above-entitled cause on April 21, 1942. (R. 102)

SUMMARY STATEMENT OF THE MATTER INVOLVED.

The petitioner, hereinafter sometimes called the taxpayer, is a Texas corporation with capital of $50,000.00 divided into 5,000 shares of no par value. Its principal asset, prior to December 1, 1937, was the Trinity Building in Ft. Worth, Texas. (R. 16)

In 1935, the Commercial Standard Insurance Company of Ft. Worth, Texas, acquired all of the capital stock of the taxpayer for $625,000.00, or $125 per share. (R. 16, 24)

During the course of an examination by the Insurance Departments of the State of Texas, Illinois, Oklahoma and Tennessee, as of December 31, 1936, the examiners suggested to the Commercial Standard Insurance Company that, in order to comply with Texas statutes, the Trinity Building, its home office building, be included in its assets as real estate instead of stock, inasmuch as the stock actually represented real estate. (R. 16, 24, 41, 48)

As a result of the above-mentioned suggestion, the following transactions occurred simultaneously on December 1, 1937:

(1) The taxpayer transferred the Trinity Building, and the lease on the ground on which it stands, to the Commercial Standard Insurance Company. The building had a depreciated cost of $617,350.54 and was encumbered by a first mortgage of $259,500.00, which was assumed by the Commercial Standard Insurance Company. (R. 17, 24) The ground lease was for a definite ten year period from December 1, 1937, with four successive options of renewal, each for a ten year period, or until 1987. (R. 46, 70)

(2) The Commercial Standard Insurance Company transferred the Reynolds-Penland Building, Dallas, Texas, to the taxpayer. The building had a basis for depreciation of $40,000.00, a depreciated cost of $263,636.16, and was encumbered by a mortgage of $150,000.00, which the taxpayer assumed. (R. 17, 24)

(3) Commercial Standard Insurance Company paid the taxpayer $60,000.00 in cash. (R. 17, 24)

(4) Commercial Standard Insurance Company transferred to the taxpayer 2,920 shares of taxpayer's own capital stock. (R. 17, 24)

At the time the exchange was made, the parties had an oral understanding regarding taxpayer's stock, which was reduced to writing in 1939 at the request of the insurance examiners. It provided that the taxpayer would set over and deliver to the Commercial Standard Insurance Company all of its 3,000[1] shares of treasury stock, as, if, and when the lease assignment of the ground lease on which the Trinity Building stands "shall fail of renewal and shall not be renewed, held and enjoyed by Commercial Standard Insurance Company during the period prior to November 30, 1987".

> "To guarantee and make certain its said obligation in regard to said stock as herein set out, Trinity Building Corporation attached hereto, and delivered herewith, certificates representing said 3000 shares of treasury stock, it being definitely understood and agreed that ownership thereof shall be, and is hereby, retained by the Trinity Life Building Corporation[2] which shall have and enjoy all the dividends, benefits, voting privileges and revenues thereof until such time as ownership may be transferred to the Commercial Standard Insurance Company under the provisions hereof.
>
> "Trinity Life Building Corporation hereby agrees that it will not cause or permit the increase, decrease or alteration of its capital stock structure, during the life of this obligation, without the consent of the Commercial Standard Insurance Company first had and obtained." (R. 24, 41, 90, 91)

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[1] 2,920 shares were transferred to the taxpayer in the transaction here involved.

[2] A former name of taxpayer.

Actually, the stock above referred to was kept in the Commercial Standard Insurance Company's lockbox at all times. (R. 42)

Taxpayer made a profit of $13,032.88 in 1930 and losses each year thereafter through 1936, aggregating $112,070.98. (R. 25) The principal of the mortgage had to be reduced $28,000.00 per year. (R. 43)

In 1938 the taxpayer sold 320 shares of its treasury stock to the Commercial Standard Insurance Company, for its book value of $73.34539 per share. The transaction was to provide the taxpayer with money to improve the Reynolds-Penland Building for a desirable long term tenant. (R. 25, 45, 49) At all times, before and after the sale, the Commercial Standard Insurance Company was the sole stockholder of the taxpayer. (R. 45, 46)

In its return for 1937 the taxpayer reported that the transactions here involved resulted in neither gain nor loss to it. (R. 25)

The Commissioner of Internal Revenue, in the notice of deficiency, divided the book value of the taxpayer's assets immediately prior to the transfer of the Trinity Building, by its 5,000 shares of authorized stock, and thus determined the value of the stock the taxpayer received in the transaction. He then valued the Reynolds-Penland Building at an appraised figure, rather than book value. The result was a determination of capital gain of $89,996.11 and deficiencies in income and excess profits taxes of $29,876.93 and $11,-259.40, respectively, most, but not all, of which are due to the adjustment mentioned. (R. 10-14, 25, 26)

Two expert witnesses testified that, even without considering the restriction on the sale of taxpayer's stock, it had no fair market value, or a very nominal value. (R. 54, 55, 63) The restriction on the sale of the stock meant that no one would purchase it. (R. 56, 63)

The Board of Tax Appeals held, despite the fact that the petitioner at all times had but one stockholder, (1) that it realized gain when it received the 2,920 shares of its own

stock and (2), the restriction on the sale of the stock did not deprive it of market value and bring it within the rule of *Helvering* v. *Tex-Penn Oil Co.,* 300 U. S. 481. The reason for this conclusion was that the stock could have been sold subject to the fifty-year restriction. The Circuit Court of Appeals affirmed.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT.

The decision below is in conflict with the established lay that "income" to be taxable must have "exchangeable value", as expressed in cases such as *United States* v. *Phellis,* 257 U. S. 156.

In the case at bar, the tax is based upon the receipt of the taxpayer's own stock from its sole stockholder. It gave up value for the stock so its assets actually were diminished. Its only hope of getting that value back into its treasury is by selling the stock, which, in turn, will create a corresponding new liability to the purchaser. Actually, therefore, the stock it received did not constitute income, because it had no "exchangeable value".

The rule is expressed by the Second Circuit in *Borg* v. *International Silver Co.,* 11 F. (2d) 147, 150:

> "They (treasury stock) are not a present asset, because, as they stand, the defendant (the corporation) cannot collect upon them. What in fact they are is an opportunity to acquire new assets for the corporate Treasury by creating new obligations."

II.

The decision below is in conflict with the established rule that "the income tax laws are concerned only with realized gains". *Helvering* v. *Bruun,* (C. C. A. 8), 105 F. (2d) 442. "The purpose of the revenue act is to tax only gain". *Weiss* v. *Weiner,* 279 U. S. 333, 335.

In the case at bar there was no realized gain. Actually, the assets of the taxpayer were decreased. If any gain were

to be realized, it could only be by the resale of the treasury stock. As heretofore stated, such resale would result in new liabilities to the new stockholders.

III.

The transaction is not taxable under the regulations. Prior to 1934, Treasury Regulation provided that "a corporation realizes no gain or loss from the purchase or sale of its own stock". A 1934 amendment to the regulations provided for computing gain or loss "if a corporation deals in its own shares as it might in the shares of another corporation", and depending "upon the real nature of the transaction". The "real nature of the transaction" is, as previously pointed out, that nothing of "exchangeable value" was received by the taxpayer.

This Court long ago decided that a single instance of the acceptance of stock in payment of a debt with a view to its subsequent sale does not "amount to a dealing in stocks". *First National Bank* v. *National Exchange Bank*, 92 U. S. 122, 128.

An isolated transaction between a corporation and its sole stockholder certainly is not dealing "in its own shares as it might in the shares of another corporation".

> "It is at least arguable that this means to cover only speculations of a corporation, * * *" *E. R. Squibb & Sons* v. *Helvering*, (C. C. A. 2), 98 F. (2d) 69, 70.

Consequently, the transaction was merely a capital transaction which did not result in "income" under the Constitution or the amended regulations.

IV.

The decision below is in conflict with established law regarding unambiguous statutes, that:

> "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are

deemed to have received congressional approval and have the effect of law." *Helvering* v. *Winmill*, 305 U. S. 79, 83.

From 1918 until 1934 Treasury regulations provided that a corporation realizes no gain or loss from the purchase or sale of its own stock. In 1934 the regulation was amended to provide for the computation of gain or loss in certain circumstances where a corporation purchases or sells its own stock.

In *Helvering* v. *Reynolds Tobacco Co.*, 306 U. S. 110, and *First Chrold Corporation* v. *Commissioner*, 306 U. S. 117, this Court held the amended regulations could not be retroactively applied to 1929 and 1933 transactions. The Court in the *Reynolds* case specifically refused to decide if the amendment to the regulation were valid when applied prospectively. The case at bar clearly presents this vexing and unsettled question.

In the *Reynolds Tobacco* and *First Chrold* cases, the corporation's stock was purchased and resold. In the case at bar, we are concerned with an isolated acquisition of a portion of the sole stockholder's stock in exchange for a part of the corporation's assets.

V.

The decision below is in conflict with *Helvering* v. *Tex-Penn Oil Co.*, 300 U. S. 481.

In the *Tex-Penn* case certain stock was received in a reorganization, with the recipients orally agreeing that they would not sell the said stock while a banking syndicate was selling the remaining stock. The oral restriction was for 90 days and was later extended for an additional 90 days. This Court held (p. 499):

> "the shares of Transcontinental stock, regard being had to their highly speculative quality and to the terms of a restrictive agreement making the sale thereof impossible, did not have a fair market value, capable of being

> ascertained with reasonable certainty, when they were acquired by the taxpayers."

In the case at bar the stock was speculative as the company had consistently lost money after the first year of its existence. (R. 25) In addition, the stock could not have been sold to third parties for 50 years, because (1) the taxpayer was bound to deliver it to guarantee the renewal of the ground lease, (2) until 1987 the taxpayer could not increase, decrease, or change its capital structure and, (3) the restriction was required by the state insurance examiners, so had to be obeyed.

The Court below distinguished the *Tex-Penn* case by stating (R. 102):

> "However, the sale of the stock was not forbidden by the agreement; the sole effect of the restriction imposed was that a purchaser would take subject to the terms of the agreement."

We submit that it is pure nonsense to say that a stock in a losing venture and subject to the said restrictions for 50 years had a fair market value. The decision is in direct conflict with the *Tex-Penn* case.

VI.

The decision below is in conflict with the decision of the Second Circuit in *Propper* v. *Commissioner*, 89 F. (2d) 617.

In the *Propper* case, stock was received subject to a five-year restriction against sale or transfer without the written consent of the bankers. The Second Circuit reversed the Board on the authority of the *Tex-Penn* case. It is obvious that in the *Propper* case an agreement to sell subject to the restriction could have been made.

VII.

The decision below is in conflict with the decision of the Seventh Circuit in *Schuh Trading Co.* v. *Commissioner*, 95 F. (2d) 404.

In the *Schuh* case stock was received with the understanding that it could not be disposed of for six months, without the written consent of one of the parties to the transaction. On the authority of the *Tex-Penn* decision, the Board of Tax Appeals was reversed. In the *Schuh* case, as in the case at bar, the stock could have been sold subject to the restriction.

CONCLUSION.

For the reasons stated, the petition should be granted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

No. ......

TRINITY CORPORATION, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Opinion Below.

The opinion of the Board of Tax Appeals (R. 22-32) is reported in 44 B. T. A. 1219. The opinion of the Circuit Court of Appeals (R. 100-102) is reported in 127 F. (2d) 604.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered April 21, 1942. (R. 102-103) The jurisdiction of this Court is found in Section 240 of the Judicial Code, as amended by the Act of February 13, 1925.

Statement of the Case.

The facts are stated in the petition for a writ of certiorari, pages 2-5 hereof, so it will not be repeated here.

Specification of Errors.

The Circuit Court of Appeals erred:

1. In holding that shares of its own capital stock received by the petitioner from its sole stockholder represented something of "exchangeable value" and were, therefore, "income".

2. In holding that shares of its own stock received by the petitioner from its sole stockholder represented "realized gain", although the receipt of such stock merely represented the opportunity to acquire new assets for the petitioner by creating new obligations.

3. In holding that the Commissioner of Internal Revenue could, by a mere change in regulations, completely change the law regarding the tax effect of a corporation's dealings in its own stock.

4. In holding that petitioner's treasury stock, which was required to be held for the benefit of petitioner's sole stockholder for fifty years, and which was in the physical possession of the sole stockholder, could have been sold subject to the fifty-year restriction and had a "fair market value".

ARGUMENT.

"Income" to be Taxable, Must Have "Exchangeable Value."

The taxpayer at all times had but one stockholder, an insurance company. The state insurance examiners "suggested" that the insurance company's ownership of its home office building, through the medium of ownership of all of the stock in the taxpayer, should be changed so that actual title to the building would be in the insurance company. The insurance company had no alternative but to follow the "suggestion" because, if it did not do so, the state authorities would find no difficulty in invoking mandatory power. Consequently, the transactions here involved were consummated. The net result was that the assets of the

taxpayer were reduced by at least $107,850.54 and the assets of the insurance company increased in a like amount, computed as follows:

Before the transaction the taxpayer owned:		
Trinity Building	$617,350.54	
Mortgage	259,900.00	
Equity		$357,850.54
After the transaction the taxpayer owned:		
Reynolds-Penland Building.	$340,000.00	
Mortgage	150,000.00	
Equity	190,000.00	
Cash	60,000.00	250,000.00
Excess of value received over value given		$107,850.54

The petitioner also received 2,920 shares of its own capital stock, subject to the restriction that they must be held and set over to the insurance company if at any time prior to 1987 the ground lease on the ground on which the Trinity Building stood should fail of renewal.

It is obvious that the said stock did not represent "income" because it had no "exchangeable value" for these reasons:

(1) Treasury stock is not a present asset because the taxpayer cannot collect on it. It offers only an opportunity to acquire new assets for the corporate treasury by reissuing the stock. That, in turn, would create corresponding new obligations to the new stockholders.

(2) The restriction on the sale made it impossible to reissue the Treasury stock to outsiders.

The cases interpreting the constitutional permission to tax "income" have consistently held that, unless the thing received has "exchangeable value", it is not income. This is fundamental and established by the earliest income tax de-

cisions. An example is *United States* v. *Phellis,* 257 U. S. 156, wherein it was decided that a dividend paid to a stockholder in one corporation with stock in another corporation was income. The reason was that the stock received had "exchangeable value", which the stockholder could sell for money or retain. Income was defined as (p. 169):

> "a gain, a profit, something of exchangeable value proceeding from the property, severed from the capital however invested, and coming in, that is, received or drawn by the claimant for his separate use, benefit and disposal."

Another way of expressing the same thought is to make the test of income whether the taxpayer has received something out of which to pay the tax or to pay debts. *Commissioner* v. *Moore,* (C. C. A. 10), 48 F. (2d) 526, 529; *Bettendorf* v. *Commissioner,* (C. C. A. 8), 49 F. (2d) 173, 176.

In the case at bar the only way the taxpayer can use the stock to pay taxes or debts is by reissuing it. However, when that is done, an obligation will be created to the new stockholder. The receipt of the stock, therefore, is not within the accepted concept of "income".

Consideration should also be given to the fact the taxpayer and the insurance company:

> "were in substance identical because of the complete ownership and control which the latter possessed over the former, as stockholder and in other capacities. While the two companies were separate legal entities, yet in fact, and for all practical purposes they were merged, the former being but a part of the latter, acting merely as its agent and subject in all things to its proper direction and control." *Southern Pacific Co.* v. *Lowe,* 247 U. S. 330, 337.

Restriction on Sale.

A further reason why the taxpayer realized no taxable gain is that the stock could not be sold to outsiders, due to the restriction. The insurance examiners required that the

stock certificates be delivered to the insurance company and that the stock be assigned to the insurance company, if the ground lease failed of renewal or enjoyment prior to November 30, 1987. Consequently, delivery of the stock could not be made prior to 1897. The Court below held that the stock could be sold subject to the restrictions. Such a conclusion is at such complete variance with actuality as to be absurd. It is fair to assume that no Justice of this Court can recall, or can find, an instance where stock was sold subject to a fifty-year restriction similar to the one here involved. Taxes should be based on what men do, not on some theoretical possibility which, in practice, would not take place.

> "Taxation is an intensely practical matter and laws in respect of it should be construed and applied with a view of avoiding, so far as possible, unjust and oppressive consequences." *Farmer's Loan and Trust Co.* v. *Minnesota,* 280 U. S. 204, 212.

This Court has adopted a practical viewpoint in connection with restricted stock. In *Helvering* v. *Tex-Penn Oil Co.,* 300 U. S. 481, certain stock was received with the oral understanding that it would not be sold while a banking syndicate was selling the remaining stock. The oral restriction was for 90 days and was later extended for an additional 90 days. It was held that the stock had no fair market value, the Court stating (p. 499):

> "the shares of Transcontinental stock, regard being had to their highly speculative quality and to the terms of a restrictive agreement making the sale thereof impossible, did not have a fair market value, capable of being ascertained with reasonable certainty, when they were acquired by the taxpayers."

In the case at bar, the stock was speculative as the company had consistently lost money after the first year of its existence. (R. 25). In addition, the stock could not have been sold to third parties for 50 years, because (1) the tax-

payer was bound to deliver it to guarantee the renewal of the ground lease, (2) until 1987 the taxpayer could not increase, decrease, or change its capital structure and (3) the restriction was required by the state insurance examiners, so had to be obeyed.

The *Tex-Penn* decision is consistent with established law that the purpose of the revenue act is to tax only realized gain. *Helvering* v. *Bruun,* (C. C. A. 8), 105 F. (2d) 442, *Weiss* v. *Wiener,* 279 U. S. 333, 335.

The *Tex-Penn* case has been followed in *Propper* v. *Commissioner,* (C. C. A. 2), 89 F. (2d) 617 and *Schuh Trading Co.* v. *Commissioner,* (C. C. A. 7), 95 F. (2d) 404, which involved restrictions of five years and six months, respectively. In each of those cases, the stock could have been more easily sold subject to the restrictions than in the case at bar. Yet the Court below specifically refused to follow the *Tex-Penn* case because of the entirely illogical, impractical and impossible conclusion that the stock could have been sold subject to the fifty-year restriction.

Fesler v. *Commissioner,* 38 F. (2d) 155, *Newman* v. *Commissioner,* 40 F. (2d) 225, and *Wright* v. *Commissioner,* 50 F. (2d) 727, cited by the Court below (R. 102) as authority for the conclusion that a restriction may reduce, but does not destroy, the fair market value were all decided before this Court's decision in the *Tex-Penn* case.

The Transaction Is Not Taxable Under the Regulations.

Prior to 1934 Treasury Regulations provided that "a corporation realizes no gain or loss from the purchase or sale of its own stock". In 1934 the regulations were amended to read:

> "Whether the acquisition or disposition by a corporation of shares of its own capital stock gives rise to taxable gain or deductible loss depends upon the real nature of the transaction, which is to be ascertained from all its facts and circumstances * * *".
>
> "But if a corporation deals in its own shares as it might in the shares of another corporation, the resulting gain

> or loss is to be computed in the same manner as though the corporation were dealing in the shares of another. So also if the corporation receives its own stock as consideration upon the sale of property by it, or in satisfaction of indebtedness to it, the gain or loss resulting is to be computed in the same manner as though the payment had been made in any other property. * * *"

The basis of the regulation is that taxation "depends upon the real nature of the transaction, which is to be ascertained from all the facts and circumstances".

As previously pointed out, the "real nature of the transaction" is that nothing of "exchangeable value" was received by the taxpayer. The net value of its assets was reduced by the transaction. It received shares of its own stock, but could exchange them for assets for the corporate treasury only by creating new obligations. Obviously, it was a mere capital transaction which could not result in income.

The taxpayer did not deal in its own shares because it is established that a single instance of the acceptance of stock in payment of a debt with a view of their subsequent sale does not "amount to a dealing in stocks". *First National Bank* v. *National Exchange Bank,* 92 U. S. 122, 128. Likewise, an isolated transaction between a corporation and its sole stockholder is not dealing "in its own shares as it might in the shares of another". *E. R. Squibb & Sons* v. *Helvering,* (C. C. A. 2), 98 F. (2d) 69. Judge Foster, in his dissenting opinion in *Allen* v. *National Manufacture & Stores Co.* (C. C. A. 5), 125 F. (2d) 239, says: "In their ordinary meanings 'deals' and 'dealings' imply a course of business or a settled policy".

The case at bar does not come within the rule of such cases as *Dorsey* v. *Commissioner,* (C. C. A. 5) 76 F. (2d) 339, where corporations with numerous stockholders transfer title to a particular asset or assets to one or more stockholders for all of the said stockholders' stock. In such cases the corporation continues with fewer assets, but with one or more stockholders eliminated. In the case at bar,

there was always but one stockholder. Would the "income" have been correspondingly increased if the taxpayer had received 4,999 shares, instead of 2,920 shares, out of the authorized 5,000 shares?

The Commissioner is Without Power to Change a Long-Continued Uniform Construction of a Re-enacted Unambiguous Statute.

It is established that:

> "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law." *Helvering* v. *Winmill*, 305 U. S. 79.

From 1918 to 1934 Treasury regulations provided that a corporation realizes no gain or loss from the purchase or sale of its own stock. In 1934 the Regulation was amended to provide for the computation of gain or loss in certain circumstances where a corporation purchases or sells its own stock.

In *Helvering* v. *Reynolds Tobacco Co.*, 306 U. S. 110, and *First Chrold Corporation* v. *Commissioner*, 306 U. S. 117, this Court held the amended regulations could not be retroactively applied to 1929 and 1933 transactions. The Court in the *Reynolds* case specifically refused to decide if the amendment to the regulation were valid when applied prospectively. The case at bar clearly presents this vexing and unsettled question.

In the *Reynolds Tobacco* and *First Chrold* cases, the corporation's stock was purchased and resold. In the case at bar, we are concerned with an isolated acquisition of a portion of the sole stockholder's stock in exchange for a part of the corporation's assets.

The Board of Tax Appeals felt that *Helvering* v. *Reynolds*, 313 U. S. 428, compelled a conclusion contrary to that contended for here. If so, this Court should clarify the rule.

The *Reynolds* case, in dealing with the "reenactment rule", does not specifically overrule the long line of cases concerning unambiguous statutes, such as *Haggar Co.* v. *Helvering*, 308 U. S. 389, which states (p. 398):

> "It is a familiar doctrine that Congress, by re-enacting a section of the revenue act without change, approves and adopts a consistent administrative construction of it."

The *Reynolds* case dealt with an admittedly ambiguous phrase[1] so, because of the lack of specific language overruling prior cases, it must have been intended to apply only to cases where ambiguity exists.

In the case at bar, section 22 (a) is a definition of income and certainly is not ambiguous.

> "The legislative intent appears clearly expressed to include all receipts and increments of every kind and nature, which, under the particular circumstances of their realization, represent in fact *income within the meaning of the Sixteenth Amendment of the Constitution.*
>
> "It is thought that a definition expressing clearly such meaning requires no interpretive regulation to clarify an ambiguity but merely to explain and call attention of subordinate administrative officers and taxpayers to those transactions which from their nature do not result in income within the meaning of that term as used in the Sixteenth Amendment and defined in *Eisner* v. *Macomber*, or which are exempt from federal taxation as imposing a burden upon state sovereignty. Such an explanatory regulation would not directly concern the meaning of the *definition* of 'gross income' in Section 22 (a), but would relate to the meaning of the term 'income' as used in the Sixteenth Amendment and to the *constitutional restrictions thereof.*"[2]

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[1] "Its meaning in this statutory setting was far from clear." P. 433.

[2] John B. Olverson, Jr., "Tax Regulations and the Reenactment Problem". Georgetown Law Journal, Washington, D. C., March, 1942. The said article exhaustively discusses the entire problem suggested by its title.

If this Court has overruled the re-enactment rule, it means that much of the certainty has passed out of administrative law. No longer can citizens, or their attorneys, rely on long and consistent administrative and judicial interpretation of a statute. If they do, they may find that an administrative official has changed the rule after the particular transaction has occurred, irrespective of the effect on the particular citizen's person or property. And, of course, there is nothing to prevent administrative officers changing their position from year to year in the light of changing or passing public opinion. It is hard to believe that this Court has made such a drastic change in established law without specifically pointing it out by overruling prior decisions. But, no matter what was decided in the *Reynolds* case, it has no application to the facts in the case at bar, because there was no gain and because "the real nature of the transaction" provisions of the Regulation so declare.

The Decision Below is in Conflict With a Decision of this Court and With Decisions of Two Circuit Courts of Appeal.

The decision below is in direct conflict with the following decisions:

> *Helvering* v. *Tex Penn Oil Co.*, 300 U. S. 481, discussed at page 15, supra;
> *Propper* v. *Commissioner*, (C. C. A. 2) 89 F. (2d) 617, and
> *Schuh Trading Co.* v. *Commissioner*, (C. C. A. 7) 95 F. (2d) 404, discussed at page 16, supra.

The petition in this case should be granted to resolve the confusing conflict occasioned by the decisions mentioned.

CONCLUSION.

For the reasons stated, the petition for a writ of certiorari should be granted.

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July, 1942.

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CITATIONS

In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 220

TRINITY CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings and opinion of the Board of Tax Appeals (R. 23–32) are reported in 44 B. T. A. 1219. The opinion of the circuit court of appeals (R. 100–102) is reported in 127 F. (2d) 604.

JURISDICTION

The judgment of the circuit court of appeals was entered on April 21, 1942. (R. 102.) The petition for a writ of certiorari was filed on July 10, 1942. The jurisdiction of this Court is invoked under

Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the value of the taxpayer's shares received on the exchange of its real property for other real estate, cash and shares of its own capital stock, should be included in determining gain or loss on the transaction under Sections 22 (a) and 111 (b) of the Revenue Act of 1936.

2. Whether the Board of Tax Appeals erred in sustaining the Commissioner's determination of the fair market value of the stock.

STATUTE AND REGULATIONS INVOLVED

The applicable statute and regulations are set out in the Appendix, *infra*, pp. 9–10.

STATEMENT

Taxpayer is a Texas corporation having a capital of 5,000 shares of no-par stock. In 1937 its principal assets were the Trinity Building, a 16-story office building, and a ten year lease, renewable for ten year periods until 1987, of the premises on which the building was situate. At that time Commercial Standard Insurance Company owned all taxpayer's capital stock. (R. 23.)

In 1937 Commercial acquired the Trinity Building and the lease of the premises from taxpayer in order to meet the requirement of the state insurance examiners. In exchange taxpayer received

$60,000 cash, other real estate and 2,920 shares of its own capital stock. (R. 23–24.) At the same time taxpayer agreed to transfer 3,000 shares of its own capital stock to Commercial in the event that it failed to renew the ground lease, and to secure this obligation taxpayer delivered certificates representing 3,000 shares to Commercial, retaining all the dividends, benefits and voting privileges pertaining to the stock (R. 24–25).

The Board of Tax Appeals found as a fact that at the time of the exchange the 2,920 shares of taxpayer's capital stock had a fair market value of $214,168.54 or $73.34539 a share (R. 26). The Board had before it in addition to the last mentioned agreement the following data upon the question of value: In 1935 Commercial had purchased the shares for $125 per share (R. 23). In 1938 Commercial purchased 320 shares at their book value of $73.34539 each (R. 25). Commercial also declared in a report to the Treasury for the period ending December 31, 1937, that the stock had a fair market value of $125 per share (R. 25). As of January 1, 1938, the Trinity Building had a depreciated cost of slightly over $600,000 (R. 24) and was appraised at a present worth of about $730,000 (R. 32); it was encumbered by a $260,000 mortgage (R. 24). The building which it received in exchange had a depreciation cost of $263,636.16 and was encumbered by a mortgage of $150,000 (R. 24). There also is evidence that taxpayer had had no

earnings for some time and, basing their testimony primarily upon that fact, two witnesses testified as experts that the stock had no market value (R. 30–31). The Board gave no weight to their opinion (R. 31).

The Board of Tax Appeals decided that the Commissioner had not erred in determining that taxpayer realized a taxable gain upon the sale of the Trinity Building, counting the shares at a fair market value of $214,168.54 as part of the consideration received (R. 26). On appeal the circuit court of appeals affirmed (R. 102).

ARGUMENT

1. This Court has recognized expressly that the definition of gross income in Section 22 (a) is "so general in its terms as to render an interpretative regulation appropriate" to deal with the question whether a corporation realizes income upon its transactions in shares of its own capital stock. *Helvering* v. *Reynolds Co.*, 306 U. S. 110, 114. The Treasury has promulgated such a regulation. The substance of Article 22 (a)–16 of Regulations 86, was first promulgated on May 2, 1934 as Treasury Decision 4430, XIII–1 Cum. Bull. 36. It provides—

> * * * if a corporation deals in its own shares as it might in the shares of another corporation, the resulting gain or loss is to be computed in the same manner as though the corporation were dealing in shares of another. So also if the corporation receives

> its own stock as consideration upon the sale of property by it * * * the gain or loss resulting is to be computed in the same manner as though the payment had been made in any other property. * * *

In the *Reynolds* case last cited it was held that the first sentence of this interpretative regulation, although appropriate, could not be applied retroactively to years in which a contrary rule was in force.[1] But here application of the regulation is not invalid under that decision. The transaction giving rise to the tax occurred in 1937, three years after the regulation was adopted. And, it is settled that the regulations may be changed and applied prospectively notwithstanding any difference in the prior rule. *Helvering* v. *Wilshire Oil Company*, 308 U. S. 90; *Helvering* v. *Reynolds*, 313 U. S. 428; *White* v. *Winchester Country Club*, 315 U. S. 32. See *Allen* v. *National Manufacture & Stores Corp.*, 125 F. (2d) 239 (C. C. A. 5th), certiorari denied, May 4, 1942, No. 1091, October Term, 1941, and *Commissioner* v. *Air Reduction Co.* (C. C. A. 2d), decided July 16, 1942, dealing specifically with this regulation.

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[1] Treasury Regulations 74, promulgated under the Revenue Act of 1928 had provided:

"ART. 66. * * * If * * * the corporation purchases any of its stock and holds it as treasury stock, the sale of such stock will be considered a capital transaction and the proceeds of such sale will be treated as capital and will not constitute income of the corporation. A corporation realizes no gain or loss from the purchase or sale of its own stock."

As applied to the present case, moreover, the change in the regulations does not reverse the earlier practice. The present case involves an exchange of property for stock and, unlike the *Reynolds Co.* case (306 U. S. 110) not the purchase and sale of stock. Even under the regulations in effect prior to 1934 the exchange of property for stock was a taxable transaction. *Commissioner* v. *S. A. Woods Mach. Co.*, 57 F. (2d) 635 (C. C. A. 1st), certiorari denied, 287 U. S. 613; *Commissioner* v. *Boca Ceiga Development Co.*, 66 F. (2d) 1004 (C. C. A. 3d); *Dorsey Co.* v. *Commissioner*, 76 F. (2d) 339 (C. C. A. 5th), certiorari denied, 296 U. S. 589; *Allyne-Zerk Co.* v. *Commissioner*, 83 F. (2d) 525 (C. C. A. 6th); cf. *Hammond Iron Co.* v. *Commissioner*, 122 F. (2d) 4 (C. C. A. 5th).

The peculiar circumstance that in the instant case the stock was acquired from the sole stockholder does not render the regulation inapplicable. Consistently with the theory that a corporation is a separate entity and the stock a transferable property, the regulation makes no distinction between corporations with one stockholder and those with many.

2. There is also no occasion for further review of that portion of the decision below which sustained the Board's determination of the fair market value of the stock. The question was one of fact on which the finding of the Board was final if supported by substantial evidence. *Elmhurst*

Cemetery Co. v. *Commissioner,* 300 U. S. 37; *Helvering* v. *Kehoe,* 309 U. S. 277, 279; *Wilmington Trust Co.* v. *Helvering,* No. 775, October Term, 1941, decided April 27, 1942. The evidence of book values and of other sales as well as the appraisal of the assets sufficiently supports the findings of the Board. See pp. 3–4, *supra.*

There is no conflict between the decision below and *Helvering* v. *Tex-Penn Co.,* 300 U. S. 481. In that case the Court did not lay down any rule that stock, the sale of which was restricted, could have no market value. That circumstance was but one among many which led the Court to hold the Board's finding to be unwarranted; equally important was the speculative character of the venture of drilling in oil fields proven to be spotty and found later to be worthless. In the instant case the beneficial ownership was transferable subject solely to the rights of Commercial to the stock if the lease were not renewed; the pledge did not, as taxpayer argues, take all "exchangeable value" from the shares. And obviously the mere fact that there had been operating losses did not make the stock too speculative for valuation. *Propper* v. *Commissioner,* 89 F. (2d) 617 (C. C. A. 2d) and *Schuh Trading Co.* v. *Commissioner,* 95 F. (2d) 404 (C. C. A. 7th) are distinguishable on their facts for like reasons. In *Heiner* v. *Gwinner,* 114 F. (2d) 723 (C. C. A. 3d), certiorari was sought on the basis of a claim of conflict with the *Tex Penn*

and *Schuh* cases similar to the claim made here but the writ was denied, *Gwinner* v. *Heiner,* 311 U. S. 714.

CONCLUSION

The decision below was correct and there is no conflict. The petition for a writ of certiorari should be denied.

Respectfully submitted,

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JULY 1942.

APPENDIX

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

* * * * *

(b) *Amount Realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

* * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

* * * * *

Treasury Regulation 94, promulgated under the Revenue Act of 1936:

ART. 22 (a)-16. *Acquisition or disposition by a corporation of its own capital stock.*—Whether the acquisition or disposi-

tion by a corporation of shares of its own capital stock gives rise to taxable gain or deductible loss depends upon the real nature of the transaction, which is to be ascertained from all its facts and circumstances. The receipt by a corporation of the subscription price of shares of its capital stock upon their original issuance gives rise to neither taxable gain nor deductible loss, whether the subscription or issue price be in excess of, or less than, the par or stated value of such stock.

But if a corporation deals in its own shares as it might in the shares of another corporation, the resulting gain or loss is to be computed in the same manner as though the corporation were dealing in the shares of another. So also if the corporation receives its own stock as consideration upon the sale of property by it, or in satisfaction of indebtedness to it, the gain or loss resulting is to be computed in the same manner as though the payment had been made in any other property. Any gain derived from such transactions is subject to tax, and any loss sustained is allowable as a deduction where permitted by the provisions of the Act.

* * * * *

ART. 22 (a)–19. *Sale of capital assets by corporation.*—If property is acquired and later sold for an amount in excess of the cost or other basis, the gain on the sale is income. If, then, a corporation sells its capital assets in whole or in part, it shall include in its gross income for the year in which the sale was made the gain from such sale, computed as provided in section 111–113. If the purchaser takes over all the assets and assumes the liabilities, the amount so assumed is part of the selling price.

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